UNITED STATES CIRCUIT COURT OF APPEALS

NINTH CIRCUIT

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THE AETNA CASUALTY & SURETY COMPANY, a corporation,
Appellant,

vs.

THE NATIONAL BANK OF TACOMA, a National Banking Association,
Appellee.

No. ....

UPON APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE WESTERN DISTRICT OF WASHINGTON, SOUTHERN DIVISION

Brief of Appellant

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STATEMENT OF THE CASE

This is an action by appellee (plaintiff in the court below), hereinafter called the "bank," against the appellant (defendant in the court below), hereinafter called the "surety," to recover upon a bond executed by American Wood Pipe Company as principal and the Surety Company as surety to the Bank and/or Twin Harbors Lumber Company as obligees. The case was originally commenced in the State Court

of the district, but was thereafter removed to the United States District Court of the Western District of Washington upon the ground of diversity of citizenship. (Tr. p. 24.) The case was tried before the court and jury. Upon the conclusion of the bank's testimony the surety moved for a directed verdict, which motion was denied. The surety then rested without introducing any testimony, and thereupon the bank moved for a directed verdict, which was granted. (Tr. p. 116.) The jury, under the direction of the court, returned a verdict against the surety in the sum of $4244.36. (Tr. p. 50.) Subsequently a judgment in that amount was entered upon the verdict. (Tr. p. 51.) This appeal is prosecuted from such judgment.

The appellee is a national banking corporation, doing a general banking business in the City of Tacoma, Washington. The American Wood Pipe Company is a Washington corporation, whose business, prior to the time that it passed under the hands of a general equity receiver in April, 1929, consisted of the manufacture and sale of wood products, principally wood pipes. (Tr. p. 70.) Upon the 21st day of January, 1929, the bond here sued upon was executed by the Wood Pipe Company as principal and the appellant as surety. Omitting formal parts, the bond reads as follows:

"KNOW ALL MEN BY THESE PRESENTS: That we, American Wood Pipe Company, a corporation of the State of Washington with principal place of business at Tacoma, Washington, as Principal, and The Aetna Casualty and Surety Company of Hartford, Connecticut, as Surety, are held and firmly bound unto Twin Harbors Lumber Company of Aberdeen, Washington, and/or The National Bank of Tacoma, Tacoma, Washington, in the penal sum of Four Thousand and No/100 ($4,000.00) Dollars, lawful money of the United States, for the payment of which, well and truly to be made the said principal and the said Surety bind themselves, their heirs, executors, administrators, successors and assigns, jointly and severally firmly by these presents.

Signed and sealed this 21st day of January, A. D. 1929.

The condition of this obligation is such that, whereas, the said principal has accepted a written order from the Twin Harbors Lumber Company of Aberdeen, Washington and/or The National Bank of Tacoma, Tacoma, Washington, dated January 19th, 1929, for furnishing the following quantity of material:

50 M. B. M. 1½x4 8 Ft. S2S 1¼x3¾ Edges Rough at $41.50 f.o.b. Tacoma.

50 M. B. M. 1½x4 9 Ft. S2S 1¼x3¾ Edges Rough at $37.50 f.o.b. Tacoma, shipment to be made within sixty days, which order is by reference made a part hereof as fully to all intents and purposes as if set forth at length herein.

NOW, THEREFORE, if the said Principal shall supply the material in accordance with the written order, and if they will indemnify Twin

> Harbors Lumber Company of Aberdeen, Washington and/or The National Bank of Tacoma, Tacoma, Washington, against any direct or, indirect damages that may be suffered or claimed for lack of delivery of material within the time called for; and further conditioned as required by law for the payment of all laborers, mechanics, sub-contractors and materialmen, and all persons who shall supply such person or persons or sub-contractors with provisions or supplies for the carrying on of such work, and all just debts, dues and demands incurred in the performance of the work, then and in that event this obligation shall be void, but otherwise it shall remain in full force and effect." (Tr. p. 15.)

The facts upon which recovery against the surety were allowed are substantially as follows: For some years previous to the execution of this bond the Wood Pipe Company had been a heavy borrower from the bank and was also a depositor in that institution, although its balance was usually very small. (Tr. p. 50.) The loans of the Pipe Company were of two classes: (1) Open unsecured loans, and (2) loans which were secured by the assignment of the proceeds of invoices of the Wood Pipe Company covering materials delivered or to be delivered. In addition to this the Wood Pipe Company on August 8, 1921, executed and delivered to the bank a general loan and collateral agreement, which in general terms sought to pledge every chose in action of the Wood Pipe Company in

the bank's possession as security for anything due from the Pipe Company to the bank. (Tr. p. 10.) Plaintiff's Exhibit 24 (Tr. pp. 141 to 161, inc.) shows the status of the specially secured account from May, 1928, to April, 1929. Plaintiff's Exhibit 25 (Tr. pp. 162 to 165, inc.) shows the status of the unsecured open account of the Pipe Company from March, 1927, to the date of the receivership. Upon January 15, 1929, the balance due on the assigned accounts was $154,899.99, and unsecured loans amounted to $20,-000.00. Upon the date that the bond was executed the balance secured by special assignments was $160,-984.61, and the unsecured balance $20,000.00. (Tr. p. 94.) Upon January 21, 1929, the Wood Pipe Company executed and delivered to the bank its promissory note in the sum of $3375.00, which note was in the usual form. (Tr. p. 9.) Upon the back of this note there appeared the following indorsement:

"No. 75583.

THIS NOTE SECURED BY:

Shipment Number 8472.
Consignee, Twin Harbors Lbr. Co.
Destination, Chicago, Ill.
Date Shipped, Jan. 21, 1929.
Invoice $3,950.00

Less Deductions	197.50
Estimated Freight	—
Margin	377.50
Advance	3,375.00

Notify Twin Harbors Lbr. Co., Aberdeen, Wash."
(Tr. p. 10.)

Upon the same day the deposit account of the Pipe Company was credited with $3375.00. (Tr. p. 40.) The record does not affirmatively show just how this credit was used by the Pipe Company. However, when counsel for the surety in the cross-examination of the President of the bank offered to show that at the time of this credit the Pipe Company was overdrawn at the bank, and that the note and assignment was accepted to cover this overdraft, counsel for the bank objected, and this objection was sustained by the lower court. (Tr. p. 90.)

Likewise upon this date the Wood Pipe Company executed and delivered to the bank the following assignment of account:

"American Wood Pipe Co.
Tacoma, Wash., January 21, 1929.
Req. No. 1/19/28
Our Order No. 8472
Terms 2% and 5% Com.
F.O.B. our mill.
Sold to Twin Harbors Lumber Co.,
Aberdeen, Washington,
Shipped to Above at Chicago, Ill.

No. 2 Clear & Better Kiln Dried Fir S2S $1\frac{1}{4}$x$3\frac{3}{4}''$ Edges Rough $1\frac{1}{2}$x$4''$ 9 length 50,000 ft. \$41.50M

		\$2075.00	
Ditto	8	50,000	37.50M
		1875.00	
		\$3950.00	

For value received we hereby assign, sell, transfer and set over unto The National Bank of Tacoma, Tacoma, Wash., the above account together with all title and interest now or hereafter owned in the goods and merchandise for which said account was incurred.

AMERICAN WOOD PIPE COMPANY.
By VAUGHAN MORRILL.
VAUGHAN MORRILL,
President." (Tr. p. 14.)

The bank, however, did not notify the Lumber Company of the execution of this assignment. (Tr. p. 92.) The bank received nothing under the assignment or upon this note, since the Pipe Company passed into the hands of a receiver in the following April. Over the objection of the surety the bank was permitted to show by the testimony of two employees of the Twin Harbors Lumber Company that in fact the order described in the bond and in the assignment was never given by the Twin Harbors Lumber Company. (Tr. pp. 105-112.)

There is no evidence in the record to show that either the surety or its agents had any knowledge of the facts relating to the status of the accounts between the bank and the Wood Pipe Company, other than perhaps a general knowledge that the bank was a creditor of the Wood Pipe Company. The surety had no knowledge that this order had been assigned to the Bank. The application of the Wood Pipe Company for the issuance of this bond appears upon pages 118 to 131, inclusive, of the record. In this application the bond is referred to as a contract bond. (Tr. p. 118.) The names of the obligees are given as "Twin Harbors Lumber Company and/or National Bank of Tacoma," and the nature of the contract is described in the same manner as in the bond.

The bank sued to recover, not the amount advanced upon the alleged security of the bond, but the amount which would have been due had the materials been delivered, plus interest at the rate of six per cent. per annum from the date of the execution of the bond. (Tr. p. 117.) Recovery was allowed substantially as prayed for the in sum of $4244.36, such sum being the amount of the purchase price, less a dealer's commission of five per cent., and a cash discount of two per cent., and interest from the date of the ap-

pointment of a general receiver for the Pipe Company.

SPECIFICATIONS OF ERROR

The appellant assigns herein the following prejudicial errors complained to have been committed by the court below:

1. That the evidence is insufficient to sustain any recovery by the bank.

2. The court erred in refusing the motion of the surety to dismiss the action and to direct a verdict in favor of the surety at the conclusion of the evidence. (Tr. pp. 114-168.)

3. The court erred in directing a verdict in favor of the bank. (Tr. pp. 114-169.)

4. The court erred in construing the surety bond executed by the surety as a guaranty for the payment of money. (Tr. pp. 116-169.)

5. The court erred in construing the surety bond executed by the surety as a contract of indemnity. (Tr. p. 169.)

6. The court erred in refusing to hold that the bank was estopped to deny the recitals of the bond. (Tr. pp. 72-169.)

7. The court erred in permitting the bank to introduce evidence to vary the terms of the bond as follows:

a. The bank was permitted to introduce evidence that prior to the writing of the bond here sued upon it was the practice of the Wood Pipe Company to borrow money on bills of lading and assigned invoices covering goods shipped to its customers. (Tr. pp. 73-169.)

b. The bank was further permitted to introduce testimony that some time in the year 1928 the Wood Pipe Company made application to the bank for loans against shipments before the goods were manufactured and shipments actually made, and that the Pipe Company then offered to secure an indemnity bond to guaranty delivery of the goods. (Tr. pp. 74-169.)

c. The bank was permitted to introduce testimony that the officers of the bank informed the officers of the Wood Pipe Company that such bond must cover two things; first, that there was a written and enforceable order, and second, that the order would be filled according to its terms. (Tr. pp. 77-170.)

d. The bank was permitted to introduce testimony as to its construction of the bond before the bond was written. (Tr. pp. 80-170.)

e. The bank was permitted to introduce testimony that on December 26, 1928, the bank held similar bonds in the sum of $37,000.00. (Tr. p. 82.)

f. The bank was permitted to offer testimony that it expected to receive the full amount of the assigned invoice. (Tr. pp. 87-170.)

g. The bank was permitted to introduce testimony contradicting the recitals of the bond to the effect that there was a written order. (Tr. pp. 105, 108, 170.)

8. The court refused to permit the surety to show that this alleged loan to the Wood Pipe Company was simply made to cover an existing overdraft of the Wood Pipe Company, and that in fact no advance was made to the Wood Pipe Company. (Tr. pp. 90-170.)

9. Even if the bank were entitled to recover anything, the court erred in entering judgment in the sum of $4244.36 for the following reasons:

a. There was a total failure of proof as to any damage whatsoever. (Tr. p. 170.)

b. In any event, the bond could not be held liable to both obligees for any greater sum than $3375.00, with interest from date of demand, because this was the maximum amount which the bank claimed to have advanced in reliance upon the execution of the bond. (Tr. pp. 10-140-170.)

c. In any event, no interest could be charged against the surety prior to August 4, 1930, the date of the filing of the complaint in the state court (Tr. p. 10), since the bank failed to prove the date of demand, although invited by the court so to do (Tr. pp. 117-170), and the court, therefore, erred in entering judgment for such additional interest.

d. In any event, the bank was not entitled to recover against the bond in a sum in excess of $2,000.00, for the reason that the maximum amount of the bond was $4,000.00, and the bond ran to two obligees, one of whom (Twin Harbors Lumber Company) was not made a party to this action. (Tr. p. 171.)

ARGUMENT

The foregoing assignments of error involve one principal question, i. e., is there any evidence to support the judgment? If this court concludes that there is none, then the judgment must be reversed and the assignments of error under Assignment No. IX, which relate to the amount of any judgment which should be entered if one is allowed, need not be considered. If, however, the record is deemed to be sufficient to support a recovery in some amount, then there will arise the additional questions (1) should such recovery be for the amount of the invoice or the amount of the

advance (2) should any interest have been allowed previous to the date upon which the complaint was filed, and (3) in any event, could there be a recovery in excess of one-half of the amount of the bond, since the bond ran to two several obligees, one of whom is not a party to this action, and therefore not bound by the judgment?

I.

There Is No Evidence to Support the Judgment

Since the surety introduced no evidence there is no disputed question of fact in this case. The only question is one of law, i. e., is there any evidence to support the judgment, either in whole or in part? We shall consider this question first from the standpoint of the bond as written and without particular reference to the evidence. The bond first recites that the Wood Pipe Company as principal and the appellant as surety are bound unto "Twin Harbors Lumber Company of Aberdeen, Washington, and/or the National Bank of Tacoma, Tacoma, Washington, in the penal sum of $4,000.00." Then follows the following recital:

> "The condition of this obligation is such that, whereas, the said Principal has accepted a written order from the Twin Harbors Lumber Company of Aberdeen, Washingotn and/or The National

Bank of Tacoma, Tacoma, Washington, dated January 19th, 1929, for furnishing the following quantity of material:

50 M. B. M. 1½x4 8 Ft. S2S 1¼x3¾ Edges Rough at $41.50 f. o. b. Tacoma.

50 M. B. M. 1½x4 9 Ft. S2S 1¼x3¾ Edges Rough at $37.50 f. o. b. Tacoma, shipment to be made within sixty days, which order is by reference made a part hereof as fully to all intents and purposes as if set forth at length herein." (Tr. p. 16.)

These recitals definitely and conclusively establish two things: First, that the bond runs to two obligees, and second, that either both of them jointly or one of them had given to the Wood Pipe Company an order for the purchase of materials. These recitals are then followed by the conditions of the bond, which are as follows:

> "Now, Therefore, if the said Principal shall supply the material in accordance with the written order, and if they will indemnify Twin Harbors Lumber Company of Aberdeen, Washington and/or The National Bank of Tacoma, Tacoma, Washington, against any direct, or, indirect damages that may be suffered or claimed for lack of delivery of material within the time called for; and further conditioned as required by law for the payment of all laborers, mechanics, sub-contractors and materialmen, and all persons who shall supply such person or persons or sub-contractors with provisions or supplies for the carrying on of such work, and all just debts, dues and demands incurred in the performance of the work,

> then and in that event this obligation shall be void, but otherwise it shall remain in full force and effect." (Tr. p. 16.)

It will be observed that the conditions of the bond cover three possible contingencies: (1) That the obligees will be indemnified "against any direct or indirect damages that may be suffered or claimed for lack of delivery of material within the time called for"; (2) that all laborers, mechanics, etc., will be paid, and (3) that all just debts, dues and demands incurred in the performance of the work will be paid.

We understand that the bank makes no contention based upon 2 and 3 above, but rests its case entirely upon that portion of the bond by which it was indemnified against any damages occasioned by lack of delivery of material within the time specified.

In considering the effect of this language a few statements of the proper rule of construction to be applied might be noted:

> "But the true rule for the construction of such contracts is that they ought to be interpreted like other classes of contracts according to the sense and meaning of the terms which the parties have used, and the terms ought to be taken, understood and given effect in their plain, ordinary and popular sense, fairly and justly to all parties to the contract." *New Amsterdam Casualty Co. vs. Central, etc., Fire Ins. Co.,* 4 F. (2nd) 203.

Likewise in *Kentucky Rock Asphalt Co. vs. Federal Casualty Co. of N. Y.,* 37 F. (2d) 279, it was held that a compensated surety is entitled to have a contract of plain meaning interpreted according to ordinary principles.

> "The liability of a surety is measured by his contract, and, whether he is a gratuitous or compensated surety, which he is liable to the full extent thereof, such liability is strictly limited to that assumed by the terms, or, as the rule is otherwise stated, a surety is not held beyond the terms, or the strict, or the precise, or the clear, or the express terms of his contract; and the surety has the right to stand upon the strict, or precise, or the very terms of his contract; and to rely on the strict letter thereof. If the surety has indicated the manner in which the indebtedness for which he has undertaken to become liable shall be incurred, he is not liable for indebtedness incurred in another way." 50 *Corpus Juris,* Sec. 126, pp. 71-73.

> "It is urged by the lumber company that contract of a surety company is, under our statutes, an insurance contract, and should, therefore, be most strongly construed against the insurer. Granting this, a contract of insurance, like any other contract, must receive reasonable construction, and while insurance contracts are construed most favorable to the insured where the meaning of the language is doubtful, there is no application of this rule when the language has acquired by judicial construction a clear, definite meaning." *U. S. F. & G. Co. v. Calif.-Arizona Construction Co.,* 186 Pac. l. c. 506.

"Contracts of suretyship should be interpreted like other classes of contracts, according to the sense and meaning of the terms which the parties have used, and those terms should be taken, understood and given effect in their plain, ordinary and popular sense, fairly and justly to all parties to the contract." *U. S. F. & G. Co. v. Centropolis Bank,* 17 Fed. (2nd) 913, 53 A. L. R. 205.

A similar rule obtains in Washington, in which state this contract was executed.

"The rule is well settled that contracts of insurance, like other contracts, are to be construed according to the sense and meaning of the terms which the parties have used, and if they are clear and unambiguous their terms are to be taken and understood in their plain, ordinary and popular sense.

An insurance company has the right to determine for itself whom it will insure and what interest it will insure, and to provide that any change in such interest without its consent will work a forfeiture of the policy. The policy before us provides in plain and unmistakable terms that any change in interest, title or possession of the subject-matter of insurance shall avoid the policy, unless otherwise provided by agreement endorsed thereon or added thereto." *Jump v. North British, etc. Ins. Co.,* 44 Wash. 596, 87 Pac. 928.

"The principle the bonding company invokes is not based upon any rule of favoritism shown a surety. It admits that the contract is to be construed liberally. The rule of liberal construction, however, of a surety's contract simply means that the contract shall be construed as contracts generally are construed when entered into between

> parties standing on an equal footing and competent to contract; that is to say, according to its evident intent and purpose, without favoritism to either of the parties. It does not require the violation of any general principle otherwise applicable to contracts." *Puget Sound Bridge & Dredging Co. v. Jahn & Bressi,* 148 Wash. l. c. 53, 268 Pac. 169-175.

To this general rule of construction there should also be added the supplemental and explanatory rule that in the absence of fraud or mistake the parties to a bond are estopped from denying the recitals contained in the bond.

> "If in making a contract, the parties agree upon or assume the existence of a particular fact as the basis of their negotiations, they are estopped to deny the fact so long as the contract stands, in the absence of fraud, accident, or mistake. There can of course be no estoppel as to matters not included in the contract." 21 *C. J.,* Sec. 111; page 1111.

> "Estoppels by contract are of two kinds. (1) Estoppel to deny the truth of facts agreed upon and settled by the terms of the contract, and (2) estoppel arising from the acts done under or in performance of the contract." *Barton Savings & Trust Co. vs. Bickford,* 122 Atl. (Vt.) 582-585.

> "For instance, when a contract is made, and the parties thereto, as a basis therefor, assume a certain state of facts to be true, they are thereafter estopped from denying the existence of such facts, so made the bases of the contract, and it is said that in this class of estoppels 'it can seldom

> be an answer to the alleged estoppel, unlike the case of estoppel by conduct, that the party supposed to be estopped acted in ignorance of the facts or under a mistake'." *Bigelow on Estoppel,* (6th Ed. 495-6).
>
> "We are of the opinion that the only contractual obligation assumed by the sureties is that set out in the recital of the bond, which recital is binding, not only on the defendants, but on the plaintiff." *Nazareth Foundry & M. Co. vs. Marshall M. & S. Co.,* 102 Atl. (Pa.) 268-270.

Applying these two rules it is submitted that the bond here sued upon not only contains no ambiguity such as to justify explanatory evidence, but that upon the contrary it definitely fixes the status of the bank as an obligee under the bond to be that of a vendee of materials from the Wood Pipe Company. The second paragraph clearly fixes the status of both obligees as such, because it recites the existence of a specific order and the exact terms of the order. If this recital be accepted, as we claim it must be, then there is no evidence to support the judgment. The proof of the bank was that in fact it gave no order to the Wood Pipe Company, and that its only connection with the transaction was that of a general creditor of the Pipe Company. Since the bond only protected it should it order material from the Wood Pipe Company, of course, without such an order it was not damaged by

the failure of the Pipe Company to manufacture the materials.

This is not an action for fraud or for mistake, because no fraud is claimed or reformation prayed for. It is a straight legal action upon a written contract, which contract is the bond. The bond indicates that the Pipe Company had a contract with some one party separately or with two parties jointly for the manufacture of certain wood products. To insure the faithful performance of this contract the bond was given, and there was but one contract, which was identified by the bond. We here distinguish between the contract and the bond by using the word "contract" to identify the alleged order given by the bank or the Twin Harbors Lumber Company, and the word "bond" to identify the document given for the protection of the parties involved in the contract. The only evidence of the existence of the contract is the recital in the bond and an invoice which was not made a part of the bond. There is no other evidence of any promise, written or implied, on the part of the second party, which ever it may have been. We, therefore, look to the bond to ascertain the identity of the second party to the contract therein referred to. Upon this there may be some ambiguity, because the bond designates the second party to the contract as the bank or the Twin Harbors

Lumber Company or both of them jointly. There were not two second parties since there was but one alleged order for materials. The bank by its pleading and proof disclaims the recitals in the bond that the bank was the second party to the contract. By the same token the bank established the indisputable fact that it had no claim against the surety on the bond. The bond, by its every word reasonably construed, shows that its entire purpose was to protect the second party to a contract to which the Wood Pipe Company was the first party. When it was established by the pleading and proof of the bank that the bank was not the party referred to in the bond as having a contract with the Pipe Company, any ambiguity in the bond created by the use of the words "and/or" was immediately removed, insofar as any right of the bank as a party to the contract or as a party to the bond is concerned, because the bond ran to the bank and/or Twin Harbors Lumber Company, whichever had the contract with the Wood Pipe Company.

The bond did not upon its face reveal which party had the contract with the Pipe Company, and it was not necessary or material that it do so. The surety cannot be charged with misleading the bank as to whether it had a contract with the Pipe Company,

because that fact was peculiarly within the knowledge of the bank.

To support this judgment the court must (1) reject the recital in the bond which definitely fixes the status of both obligees as vendees of goods to be manufactured by the Pipe Company, and (2) import into the bond an obligation of the surety in nowise expressed therein, either expressly or by necessary implication. This the pleadings and proof do not permit the court to do. The action was one upon the bond as written, and no fraud or mistake was alleged or reformation asked for. The document is plain as to the obligation of the surety. Since no legal reasons exist to require or even justify either reformation or construction, the action must fall under the bank's own proof.

Any considerable discussion of the evidence, therefore, becomes unnecessary, since it cannot be claimed that there is anything in the record which supports any judgment if our construction of the bond be adopted. The evidence does no more than to establish the fact that the bank was a creditor of the Pipe Company; that as collateral security for a loan, made possibly to cover an existing overdraft, it took an assignment of the proceeds of this order, and that the loan

has not been paid. Incidentally it might be observed that the Surety Company was not permitted to show by cross-examination of the President of the bank that this advance was made to cover an overdraft (Tr. p. 90), and also that the bank did not notify the Twin Harbors Lumber Company that this account had been assigned to it. (Tr. p. 92.) It would seem that this latter fact was a rather unusual practice if the transaction was what it purported to be upon the books of the bank. Be that as it may, however, we think all this evidence is entirely immaterial. It simply went to an independent collateral transaction which had no relationship to the obligation of this bond. For this reason it is unnecessary to specifically discuss the various particular assignments of error which relate to the introduction of this testimony.

We anticipate that the bank will make much of the decision of the State Supreme Court in the case of *National Bank of Tacoma vs. Aetna Casualty & Surety Company,* 161 Washington, 239, 296 Pac. 831, in which case a department of the Washington Supreme Court, with the Chief Justice dissenting, allowed a recovery upon a similar bond between the same parties, which was made at about the same time.

The Washington case, insofar as the ultimate result is concerned, is authority for the allowance of a

recovery upon this bond, but it is not a precedent for the legal conclusion reached by the court below, or for the recovery of anything in excess of the actual advance made. The complaint in the Washington case, as appears from Page 833 of the decision as reported in the Pacific Reporter, was drawn upon the same theory as is the complaint herein, and there, as here, judgment was prayed for the full invoice price. The complaint was not drawn upon the theory that it was an indemnity bond or that the advance was made for the purpose of providing funds to the Pipe Company to manufacture the goods described in the bond. Neither was any such argument made by the bank in its brief, a fact conceded by the state court in its opinion when it said (Page 833):

> "The discussions by counsel for both parties go far afield in citing and discussing many texts and authorities not apposite to this case."

The state court held (1) that the bond was an indemnity and not a surety bond, and (2) that the advance made by the bank was for the specific purpose of furnishing funds to the Pipe Company with which to execute this order. Based upon these two propositions recovery was allowed in the amount of the special advance, less a partial payment made by the Twin Harbors Lumber Company.

In the present case recovery was allowed for the full amount of the invoice, a conclusion necessarily inconsistent with that of the state court that the purpose of the bond was to protect loans of money put up to complete the contract. The Washington case, therefore, is not authority which supports this judgment, although if followed it could be made the basis of a judgment in favor of the bank in a different amount.

The reasoning of the Washington court is difficult to follow. Much importance is apparently attached to its conclusion that the bond is one of indemnity. Even if that be admitted we cannot understand its materiality. Whether we call it indemnity or something else the recovery under it would be the same, i. e., as stated in the bond. Neither can the terms of an indemnity bond be varied by parol evidence any more than any other written document.

As an academic proposition, however, it is submitted that this conclusion of the Washington court is erroneous. This conclusion is based upon the following quotations from 14 *R. C. L.* 44:

> "There is an obvious and important difference between a contract of guaranty or suretyship and a contract of indemnity." (Opinion p. 833.)

The writer of the opinion should have quoted the remainder of this paragraph in 14 *R. C. L.,* which is as follows:

> "The former type of contract is a collateral undertaking and presupposes some contract or transaction to which it is collateral, while the latter is essentially an original contract."

Reading this bond according to its ordinary meaning it cannot be doubted that it was an undertaking collateral to the principal contract described therein, and that the right to recover upon the bond depended entirely upon the performance or nonperformance of the principal contract of the Pipe Company. In the face of this recital in the bond, how can it be said that this was an original undertaking and not one collateral to the performance of another contract?

See also *Abrahamson vs. Burnett,* 157 Wash. 668-671, 290 Pac. 228, where this quotation was set forth in full.

In *Stearn on Suretyship* (3rd Ed.), Sec. 32, Page 37, it is said:

> "The latter undertaking (indemnity contract) is an engagement to make good or save another from a loss upon some obligation which he has or is about to incur to a third party *and is not a promise made to one to whom another is answerable.* In other words, the promise is to the debtor and not to the creditor. There is no apparent dif-

> ference in principle between a promise to a debtor to pay his obligation and a promise to indemnify him against it." (Italics ours.)

This bond was a promise made to one to whom another was answerable, i. e., it was a promise made to the lumber company and/or the bank to whom the Pipe Company was answerable. The promise was to the vendee and not to the vendor, because the Pipe Company was the vendor and to it no promise was made. How then can it be said that this is a bond of indemnity?

Likewise in Vol. I, *Brand on Suretyship* (3rd Ed.), Page 19, it is said:

> "Contracts of suretyship and guaranty are both to be distinguished from contracts of indemnity. In a contract of indemnity, the indemnitor, for a consideration, promises to indemnify and save harmless the indemnitee against liability of the indemnitee to a third person or against loss resulting from such liability."

Where in the four corners of this bond is there anything whereby the surety agreed to indemnify the bank against liability to a third party or against loss resulting from such liability. Nowhere does the bond indicate that any liability to a third party was to be assumed by the bank.

See also 20 *Cyc.* 1402, and *Hall vs. Equitable Surety Company*. 191 S. W. 32.

The opinion of the Washington Court nowhere explains or disposes of the recital in the bond that an order had been given to the Pipe Company by the bank and/or the lumber company. Upon the contrary the Washington Court erroneously stated the conditions of the bond when it said (Opinion, Page 834):

> "The surety company gave a bond, a condition of which is that, whereas, the principal has accepted a written order from the Twin Harbors Lumber Company, now if the pipe company will supply the material in accordance with the written order to indemnify the bank against any direct or indirect damages which may be suffered by a lack of delivery of material within the time specified, then the bond to be void."

This is an erroneous statement of the conditions of the bond, because it disregards and omits the clause "and/or the bank." The entire conclusion of the Washington Court, therefore, is based upon a construction of the bond which is opposed to its language, and hence the decision is not sound.

A few other inaccuracies in the opinion may be noted. For instance, upon Page 834 it is said:

> "Obviously, however, appellant's agents knew full well that the bank did not manufacture lumber and lumber products and that its principal

> did. Without any evidence, they knew that the sole business of the bank was loaning money."

If this conclusion had any substantial weight in the ultimate decision it certainly was erroneous. The bond recites that in this instance either the bank or the lumber company or both had purchased materials from the pipe company, an occupation different from the loaning of money. By its acceptance of the bond the bank acknowledged the correctness of this statement. Furthermore, as incidental to the loaning of money, banks may, and often do, engage in other transaction. For instance, the lumber company might have been a debtor of the bank and the bank might have held an assignment of the claim of the lumber company as collateral for the loan. If such a situation had existed the inclusion of the bank as a principal obligee would have been quite consistent and reasonable.

Again in its decision the Washington Court said (Opinion, Page 835):

> "Thus for nonfulfillment of the order to the lumber company, the pipe company would be liable for damages measured by the difference between the value of the goods at the date of the breach of the bond and their value to the lumber company had they been constructed and delivered within the time agreed. This is uniformly settled by our own cases and by the courts of other states very generally."

We submit that there is nothing in the bond or in the record which justifies the placing of these two obligees in two different classes. The language of the bond is identical as to both. Both of them by the same language are given the status of vendees of the Pipe Company, and both of them are protected against any damage sustained as the result of the non-delivery of the materials to them as such vendees. If the measure of damages as to the Pipe Company is as stated by the Washington Court, then where in the bond or in the record, is there any justification for the application of an altogether different and more favorable rule in behalf of the bank? To do so is to vary and contradict the terms of the bond, a subject which the decision of the Washington Court very carefully avoids.

It is submitted that the judgment should be reversed and the action ordered dismissed in its entirety.

II.

In Any Event No Recovery Should Have Been Allowed in Excess of the Advance Made by the Bank

If the court agrees with what has already been said, the judgment must be reversed and the remainder of this brief may be disregarded. In the event, however, that the court should conclude that a recov-

ery should be allowed, it is submitted that in no event could such recovery exceed the amount of the advance. The judgment of the court below allowed recovery in the amount of the invoice ($3950.00), less seven per cent. for commissions and discounts, or $3673.50, plus interest from the date of the receivership of the Pipe Company, or a total of $4244.36. (Tr. pp. 112-114.) The actual advance made by the bank was $3375.00. (Tr. p. 9.) The surety contends that recovery in the principal sum could not exceed this advance, irrespective of interest. Therefore, the judgment was in any event excessive in the sum of $298.50, this being the difference between the amount allowed by the lower court and the actual advance. We think little argument is necessary on this point. The bank does not contend that it purchased the proceeds of this order from the Pipe Company. Upon the contrary, it took the note of the Pipe Company for $3375.00 (Tr. p. 9), which was secured by an assignment of the proceeds of the order. (Tr. p. 14.) The only damage then which under any view it could be claimed that the bank sustained was occasioned by the failure of the Pipe Company to pay the note, which was $3375.00, and not $3673.50.

This was the conclusion reached by the State Court in the case of *National Bank of Tacoma vs. Aetna*

Casualty & Surety Company, supra. In that case the amount of the invoice, less deductions, was $2730.00, for which amount the bank sued. The amount of the advance was $2235.00. The sum of $974.79 was paid upon the partial delivery of the order by the Pipe Company, and recovery was allowed for the unpaid balance of the advance, and not the unpaid balance of the invoice price. (Opinion, p. 834.)

We do not overlook the fact that in 1921, some eight years prior to this time, the Pipe Company executed and delivered to the bank a so-called general loan and collateral agreement. (Tr. p. 10.) The inability of the bank to collect and apply this excess of $298.50 upon other general obligations of the Pipe Company, if any intent so to do ever existed, could by no stretch of the imagination be deemed a damage "for lack of delivery of material within the time called for." To so hold would be to inject into the transaction, as an item of damage, a wholy independent transaction. Moreover, the fact that here there was a specific note for $3375.00, accompanied by an assignment of this account, would seem to remove the transaction from the scope of the general collateral agreement, which would of necessity limit the bank's loss to the advance actually made upon the security of the assignment. If this was not the intent of the

parties, then why was it necessary to take this note and specifically assign this account as collateral?

III.

Interest Should Not Have Been Allowed Prior to August 4, 1930

The lower court allowed interest upon the invoice price, less deductions, from April 18, 1929, the date upon which a receiver was appointed for the Pipe Company. (Tr. pp. 59-115.) The complaint alleged that demand was made previous to suit, but did not set forth the date of such demand. (Tr. p. 39.) No evidence was offered upon this point, although this was called to the attention of counsel for the bank after the motion for a directed verdict by the bank had been granted. After the jury had been instructed to return a verdict for the bank, but before the verdict had been returned, counsel for the surety excepted to the instructed verdict — among other things: "Fourth, for the further reason that interest is not recoverable except from the date that demand was made upon the surety company, as held by the Supreme Court of this state." (Tr. p. 117.) Thereupon the following occurred:

> "The Court: The plaintiff did not show the date of demand, as I recall. Plaintiff asked to show when demand was made?

Mr. Metzger: No, your Honor. I think we are entitled to interest as calculated." (Tr. p. 117.)

The record failing to show the date of demand, it is submitted that interest should not have been charged for any period prior to August 4, 1930, the date when the complaint was filed in the state court. (Tr. p. 14.)

While there is some conflict of authority in other jurisdictions concerning the question of when interest begins to run, the Washington Court in *National Bank of Tacoma vs. Aetna Casualty & Surety Company, supra,* announced the rule which we contend for in the following language (Opinion, p. 835):

> "As a necessary part of his damages, an indemnitee may also recover against his indemnitor interest after due notice to the indemnitor of the loss and damage."

In *Illinois Surety Company vs. John Davis Co.,* 244 U. S. 376; 61 Law Ed. 1206, it was said:

> "The contract and bond were made in Illinois and were to be performed there. Questions of liability for interest must, therefore, be determined by the law of that state."

The rule announced by the Washington Court must, therefore, be applied herein.

This rule is in accord with the following decisions of the Federal Court:

In re Perelstine, 44 Fed. (2nd Ed.) 1019;

Black Diamond SS. Corporation vs. Fidelity & Deposit Co. of Maryland, 33 Fed. (2nd Ed.) 767.

IV.

The Judgment Should in No Event Have Been for More Than One-Half of the Penalty of the Bond with Interest

This bond is in the penal sum of $4,000.00. (Tr. p. 15.) It runs to two obligees, one of whom is not a party to this action. Upon its face it may be either joint or several. It cannot be both. As was said in 9 *Corpus Juris* 38:

> "A bond given to two or more obligees may be given to them jointly or severally, but not jointly and severally."

See also:

Title Guaranty & Surety Co. vs. Foster, 203 Pac. 231 (Okla.).

The proof shows that this bond was not a joint obligation because the bank by its pleading and proof established the fact that it did not have any contract with the Pipe Company either by itself or jointly with the lumber company, and further established the fact that the lumber company was in no way connected with the transactions upon which a recovery was allowed. The bond then was a several obligation running

to the Lumber Company and the bank. The lumber company was not a party to the action, and is not bound by the judgment. Consequently, one-half of the amount of the penalty of the bond should be reserved to protect what, if any, rights the lumber company may have arising out of any separate transaction with the Pipe Company.

Substantially all of the authorities upon this are referred to and discussed in *Title Guaranty & Surety Co. vs. Foster,* 203 Pac. 231. That case involved a guardian's bond given to cover the accounts of five wards. In an action in behalf of one of the wards, to which action the others were not made parties, it was held that the recovery could not exceed one-fifth of the penal sum of the bond.

This decision was subsequently reaffirmed by the same court in *Southern Surety Co. vs. Williams,* 231 Pac. 293.

Likewise the same rule has been followed in Iowa and Wyoming.

Hooks vs. Evans, 68 Iowa 54; 25 N. W. 925-926;
U. S. Fidelity & Guaranty Co. vs. Parker, 121 Pac. 531; 124 Pac. 269.

We anticipate that these cases may be attempted to be distinguished by reason of the fact that in this

case one M. H. Williams, office manager of the lumber company, and one Tully Stallard, an auditor for the same company, testified that the lumber company had never given the order referred to in the bond. (Tr. pp. 101 to 113.)

This testimony we submit does not change the situation. The admissions of these employees of the lumber company, which is a corporation, cannot bind that corporation as a matter of law, since the corporation is not made a party to the action. As was said by the Iowa court in *Hook vs. Evans, supra* (p. 926), "The other three wards were not made parties, and without them no judgment can be rendered by which their rights can be impaired."

Furthermore, those admissions go no further than to negative the existence of any liability to the lumber company as a vendee of materials to be manufactured. The language of the bond is identical as to both the lumber company and the bank. If the bank is entitled to recover as a creditor of the Pipe Company, by the same token the lumber company could likewise recover upon a similar state of facts. Neither of these witnesses testified to anything except the nonexistence

of the order referred to in the bond. It is therefore submitted that recovery could in no event exceed one-half the penalty of the bond, which is $2000.00, plus interest.

Respectfully submitted,

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